

service

Department of the Treasury

DEN 0254

31 Hopkins Plaza, Baltimore, MD 21201

Person to Contact:

Telephone Number:

Refer Reply to:

Date: OCT 3 1997

CERTIFIED MAIL

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(c)(7) of the Internal Revenue Code.

The information submitted indicates you were incorporated under the laws of [REDACTED] on [REDACTED].

Your stated purpose is to promote and encourage the social and fraternal aspects of its members' lives through healthy social interaction.

Membership qualifications are based on an annual membership fee of \$[REDACTED] or a lifetime fee of \$[REDACTED]. Outside of payment of said dues, there are no restrictions imposed except that the membership committee, evaluates each potential member as regard to his or her personality, interests, and social compatibility with the existing membership.

The organization's receipts are derived primarily from food and beverage sales and video machine income. In addition, the organization reported amounts earned as interest on its checking account.

The organization's financial statements reflect amounts incurred or expended for the following:

- a) salaries, wages and other compensation
- b) taxes and licenses
- c) utilities
- d) occupancy
- e) sales tax
- f) contract services
- g) supplies
- h) accounting fees
- i) equipment rental and maintenance
- j) bank charges, and
- k) other miscellaneous expenses

Section 501(c)(7) of the Internal Revenue Code exempts from federal income tax, clubs organized for pleasure, recreation, and other non-profitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inure to the benefit of any private shareholder.

Section 1.501(c)(7) of the Income Tax Regulations provides . . follows:

- a) The exemption provided by section 501(a) for organizations described in section 501(c)(7) applies only to clubs which are organized and operated for pleasure, recreation, and other non-profitable purposes, but does not apply to any club if any part of its net earnings inure to the benefit of any private shareholder. In general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues, and assessments. However, a club otherwise entitled to exemption will not be disqualified because it raises revenues from members through the use of club facilities or in connection with club activities.
- b) A club which engaged in business, such as making its social and recreational facilities available to the general public, is not organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, and is not exempt under section 501(a). Solicitation by advertisement or otherwise for public patronage of its facilities is prima facie evidence that the club is engaging in business and is not being operated exclusively for pleasure, recreation, or social purposes.

Public Law 94-568 as explained in Senate Report No. 94-1318, published in Cumulative Bulletin 1976-2, page 597, provides that a club exempt from taxation and described in section 501(c)(7) is to be permitted to receive up to 35% of its gross receipts from a combination of investment income and receipts from non-members (from the use of its facilities or services) so long as the latter do not represent more than 15 percent of the total receipts. It is further stated that if an organization exceeds these limits, all of the facts and circumstances must be considered in determining whether the organization qualifies for exemption.

While there is no statutory definition of "club" as used in IRC 501(c)(7), it implies the existence of personal contact, commingling and fellowship among members. In addition to personal contact among members, the term "club" presupposes the existence of a common objective among members. In other words, passive association is not enough; members must be joined by a mutuality of active interests or shared goals justifying the existence of the organization.

Revenue Ruling 69-635 of Cumulative Bulletin 1969-2, page 126 discusses the requirement of personal contact and commingling. In this instance, the organization provided various motoring conveniences to its members. It entered into arrangements with numerous garages across the country whereby emergency repairs and road services were furnished to the members and paid for by the organization. It also provided rewards for recovery of stolen vehicles, posted bonds in the event of an arrest of a member, provided travel information, and arranged for reduced premiums on automobile insurance.

The organization failed to qualify for exemption under 501(c)(7) based on the lack of personal contact and commingling. In addition, the services provided were not in the nature of pleasure or recreation but rather, a type generally available on a commercial basis.

Revenue Ruling 67-139 of Cumulative Bulletin 1967-1, on page 129, provides an example of an organization sharing common objectives and mutuality of interests. The instant organization was formed by mineralogy and lapidary enthusiasts to disseminate knowledge of mineralogical and lapidary subjects, to promote their application so that greater pleasure may be derived from the activities, and to promote good fellowship among its members.

The club held monthly social meetings during which the members discussed gem and mineral topics, and sold, purchased, or exchanged rock and mineral specimens; issued a bulletin containing news of members' social activities and their rock and mineral collections; and conducted an annual show for the public where members displayed their lapidary techniques and mineral specimens.

In providing a meeting place for its members where they associate with each other, enabling them to be more proficient in their hobbies, and operated primarily to accommodate its members in their recreational pursuits, the club accordingly, qualified for exemption under 501(c)(7).

Revenue Ruling 58-588 of Cumulative Bulletin 1958-2, page 265 discusses an organization formed by several individuals to operate a health, recreation and social club but whose predominant activity was the selling of services for profit to an unlimited number of so-called "members" who had no voice in the management of the club and whose only rights were to use the club's facilities upon the payment of specified fees.

The organization was incorporated as a non-profit membership corporation without capital stock. Its purposes were to operate a health, recreational and social club, including a clubhouse, restaurant, gymnasium, baths, and recreational facilities. Its bylaws provided for two classes of memberships, active and associate. The then current membership, consisted of 25 active members and approximately 25,000 associate members.

The active members had exclusive voting rights, while the associate members had only the right to use the club facilities.

The organization was managed and controlled by a board of directors elected from and by the active members. The officers of the organization were elected from among the board of directors. The board of directors functioned as a membership committee, and any one of them could exercise the functions of the committee for the purpose of receiving applications for associate membership. In addition, any member of the membership committee could summarily revoke an associate membership at his discretion without assigning any reason thereto. The club was determined not to be a tax-exempt social club under section 501(c)(7) of the Internal Revenue Code.

In Revenue Ruling 66-225, Cumulative Bulletin 1966-2, page 227, an organization providing entertainment for its members, but controlled by a taxable corporation and operated as an integral part of such corporation's business, was held not to qualify for exemption under section 501(c)(7).

The club's articles of incorporation state that its purpose was to operate a private club for its members and to provide entertainment, food and refreshment for them. This club had three classes of memberships: (1) An annual dues paying membership; (2) a 90-day membership; and (3) a weekly membership for persons temporarily residing at an adjoining motel.

The club had a dining area and a cocktail lounge. The club's patrons were permitted to bring liquor and alcoholic beverages to the club. This club was determined not to be operated exclusively for pleasure, recreation, and other non-profitable purposes, and accordingly did not qualify for exemption under section 501(c)(7) of the Code.

The determination as to whether a particular organization is a club in the sense of the statute often depends on criteria other than the relationship of its members to each other. Where membership requirements are broad or vaguely stated and the initiation charges or dues are low enough that one-time or transient use of the facilities by the general public is encouraged; or where management is strenuously engaged in expanding club membership and can effectively perpetuate itself through close physical and financial ties to club activities, or by other means, consideration must be given as to whether the organization is a business operation rather than a club.

Information submitted with your application indicates that there is a single officer/director/trustee/manager, though your bylaws provide for a President, Secretary and Treasurer. In addition, while indicating membership fees to be a source of financial support, no such amounts were reflected in your financial statements.

[REDACTED]

In your response to our request for information, you offered the following information:

- While indicating only one class of membership, membership is essentially open to anyone paying the annual or lifetime membership fee. The members total approximately [REDACTED] individuals.
- Membership in the club is contingent upon the membership committee's acceptance of applicant's based on personality, interests and social compatibility with the existing membership, and thus subject to automatic revocation, if not in abidance with bylaws or rules of the organization, based on the sample membership application submitted.
- Concerning the frequency with which members meet to discuss the business affairs of the organization, you indicate that members meet annually to elect officers, however the officers meet as needed for day to day operation of the club.

As was the case in Revenue Ruling 67-139, your organization lacks the requisite elements of shared common objectives and mutuality of interests. Therefore, although "members" gather in a social setting, this passive association, in and of itself, is not sufficient, barring any mutuality of active interests. In addition, as was the case in Revenue Ruling 69-635, the services or activities provided by your organization are in the nature of the type provided generally on a commercial basis.

Further, your government mirrors that illuminated in Revenue Ruling 58-588.

While you indicate having only one class of membership, you are governed essentially by a limited group, if not a single individual, determining membership suitability and the "members" possess no rights other than use of the facility. This is evident based on the infrequency with which you meet other than to eat, drink and to engage in entertainment.

We consider your membership requirements to be broad or vaguely stated and, that transient use by the general public is encouraged, since the membership fee is relatively low. Moreover, the club's perpetuity, is reliant on the expansion of membership as well as to the close physical and financial ties to club activities. We believe your activity constitutes a subterfuge for doing business with the public.

On the basis of the evidence presented, the requirements for exemption of a social and recreational club as defined in the Code and Regulation cited in the Revenue Rulings, we conclude that your "club", as was the case in Revenue Ruling 66-225, is not operated exclusively for pleasure, recreation or other non-profitable purposes as described under section 501(c)(7). We therefore hold, that you do not qualify for exemption under this section or any other section under 501(a).

[REDACTED]

Until you have established an exempt status, you are not relieved of the requirements for filing Federal income tax returns.

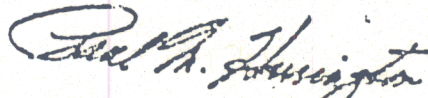
If you do not agree with our determination, you may request consideration of this matter by the Office of Regional Director of Appeals. To do this, you should file a written appeal as explained in the enclosed Publication 892. Your appeal should give the facts, law, and any other information to support your position. If you want a hearing, please request it when you file your appeal and you will be contacted to arrange a date. The hearing may be held at the regional office, or, if you request, at a mutually convenient district office. If you will be represented by someone who is not one of your principal officers, that person will need to file a power of attorney or tax information authorization with us.

If you don't appeal this determination within 30 days from the date of this letter, as explained in Publication 892, this letter will become our final determination in this matter.

Appeals submitted which do not contain all the documentation required by Publication 892 will be returned for completion.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely yours



Paul M. Harrington
District Director
Southeast Key District

Enclosures:
Publication 892

CC: [REDACTED]